ORDER NO. 16 419

ENTERED OCT 27 2016

BEFORE THE PUBLIC UTILITY COMMISSION

OF OREGON

UE 308, UI 376

In the Matter of PORTLAND GENERAL ELECTRIC COMPANY, 2017 Annual Power Cost Update (Schedule 125) (UE 308), and Application for Affiliated Interest Transactions and Request for Waiver of OAR 860-027-0048(4)(e) (UI 376).	ORDER

DISPOSITION: STIPULATION ADOPTED; NET VARIABLE POWER COSTS AND ANNUAL UPDATE TARIFF TO BE REVISED; LONG-TERM HEDGING COSTS REJECTED; AFFILIATED INTEREST TRANSACTIONS AND REQUEST FOR WAIVER DENIED; SUPPLEMENTAL ORDER TO BE ISSUED

I. SUMMARY

In this order, we adopt the stipulation of the parties regarding Portland General Electric Company's (PGE) 2017 proposed Net Variable Power Costs (NVPC) and the Annual Update Tariff (AUT). The AUT is designed to allow PGE to revise customer rates to reflect those changes in its projected NVPC resulting from new information. We order PGE to file new tariffs reflecting the modifications and conditions set forth in the stipulation.

We decline to approve PGE's long-term natural gas hedging proposal that includes the creation of a wholly owned subsidiary that will have a non-operating working interest in well exploration, drilling, development, and operation. Due to time constraints, we will issue a supplemental order providing our rationale for declining PGE's request. In light of this decision, we also deny PGE's application, as submitted in docket UI 376, for approval of the affiliated interest transactions associated with this proposal and waiver of OAR 860-027-0048(4)(e) (the lower-of-cost-or-market rule) for purchases from the subsidiary.

II. PROCEDURAL HISTORY

On April 1, 2016, PGE filed its forecast of the company's 2017 NVPC under the terms of its AUT (Schedule 125). PGE's filing also included a long-term hedging proposal. PGE proposed that costs associated with this long-term hedging would be included in the calculation of NVPC, starting in this 2017 AUT. PGE requested that we allow the inclusion of these costs in the 2017 AUT. In related docket UI 376, PGE requested that we approve the associated affiliated interest transactions and waive the lower-of-cost-or-market rule for purchases by PGE from its new subsidiary.[1]

We adopted two schedules in this docket, one for the long-term hedging proposal, and the other for all other power cost issues. The schedules contemplated addressing all issues not related to the long-term hedging proposal and resolving them at an early date. Open issues with respect to long-term hedging would be addressed thereafter.

Pursuant to that schedule, Staff of the Public Utility Commission of Oregon, the Citizens' Utility Board of Oregon (CUB), and the Industrial Customers of Northwest Utilities (ICNU) filed testimony on general power cost issues.

On June 27, 2016, PGE, Staff, CUB, and ICNU held a settlement conference. Thereafter, PGE filed a motion to suspend the power cost procedural schedule, indicating that the parties had reached agreement in principle. The administrative law judges granted the motion.

On August 18, 2016, PGE filed a stipulation joined by Staff, CUB, and ICNU.[2] A copy of the stipulation is attached as Appendix A. The stipulation settles all issues raised in these proceedings except those regarding the long-term hedging proposal. Also on August 18, 2016, PGE, Staff, CUB, and ICNU filed testimony in support of the stipulation. The stipulation and supporting testimony are admitted as evidence in this proceeding.

On June 3, 2016, PGE filed supplemental hedging testimony. On August 12, 2016, pursuant to the agreed upon schedule, the parties filed reply hedging testimony and PGE filed rebuttal hedging testimony on September 2, 2016. A hearing was held on September 21, 2016. Opening briefs were filed on October 3, 2016, and reply briefs were filed on October 11, 2016.

III. BACKGROUND

Annually, PGE files its forecast of the company's upcoming NVPC under the terms of its AUT. NVPC include wholesale power purchases and sales, fuel costs, and other costs that generally change as power output changes. The AUT is designed to allow PGE to annually revise customer rates to reflect changes in its projected power costs resulting from new information. The updated power cost forecast will also be used as the baseline for comparing actual NVPC

[1] To align the timing of our decisions on the affiliated interest transactions and the overall long-term hedging proposal, PGE withdrew the affiliated interest application it initially filed in docket UI 371 and then resubmitted it later in docket UI 376.

[2] Noble Americas Energy Solutions, LLC, filed a petition to intervene, but did not otherwise participate in the docket. Noble does not object to the stipulation.

when PGE applies the Power Cost Adjustment Mechanism (PCAM) set forth in its Annual Power Cost Variance tariff.

In its initial filing, PGE presented its initial 2017 NVPC forecast of $423.6 million, or $26.34 per MWh. The 2017 NVPC forecast was $423.6 million, net of production tax credits. This is approximately $1.80 per MWh less than the final forecast for 2016. PGE estimated a base rate impact of a 1.4 percent reduction. The lower overall forecast for 2017 compared to 2016 is largely due to increased market purchases and lower contract costs. Slightly higher net resource costs and an increase in transmission costs (largely attributable to including the fixed transmission costs for the Carty Generating Station in each month of the forecast year) partially offset the power cost decrease.

On July 15, 2016, PGE filed an update of its 2017 NVPC, including contracts and electric and gas forward curves as of June 2, 2016. The result is a reduction of $18.8 million to $404.7 million. PGE explains this decrease is primarily due to a reduction in the power cost impacts associated with PGE's long-term hedging proposal.

IV. STIPULATION ADDRESSING GENERAL AUT ISSUES

The parties agree that the stipulation settles all issues in this docket except those regarding the long-term hedging proposal. Specifically, the parties agree to the following for the purposes of this docket:

A. Portland Hydro Project (PHP) Power Purchase Agreement (PPA) Expiration

1. Parties' Original Positions

The PHP is a hydroelectric power generating facility located in the Portland-owned Bull Run watershed. The City of Portland sells the power output to PGE under a PPA. The agreement expires on August 31, 2017. Under the PPA, PGE could receive a disbursement in 2017 from a renewal and replacement fund created under the agreement. Because PGE's receipt of a disbursement is not certain, PGE did not include the payment in its forecasted NVPC calculation.

Staff proposed that 100 percent of any disbursement PGE receives in 2017 in connection with the termination of the PHP agreement be flowed through to customers by deferring any disbursement rather than capturing it in the PCAM, which trues up forecasted NVPC to actual subject to a deadband, sharing, and earnings test.

2. Stipulated Agreement

Forecasted costs will reflect the assumption that PGE will receive a refund of $9.4 million from the City of Portland related to the expiration of the PHP PPA. If PGE receives a different amount in 2017 or 2018, the difference between this forecasted amount and the actual amount received will be included, with interest, in PGE's 2019 AUT.

B. PHP PPA Price

1. Parties' Original Positions

The PHP contract contains complicated pricing terms and is based on the actual embedded cost of the hydroelectric facilities, plus a "share-the-savings" component. That component was calculated based on the difference between the embedded PHP facilities costs and the embedded cost of the Colstrip Generating Station Units 3 and 4, which were once considered to be marginal resources for PGE. The relative savings are split between the City of Portland and PGE, resulting in an increase in the price paid by PGE when the share-the-savings element is positive. The price is not reduced when the savings are negative to the point that the pricing is below the embedded costs of the PHP. Instead, that amount carries forward and eventually accrues to a "Renewal and Replacement Fund," which is to be settled financially upon the termination of the contract.[3]

Staff proposed that PGE defer any revenue that it might receive in 2017 from the PPA rather than allowing the revenue to flow through to customers through the PCAM subject to a deadband, sharing, and earnings test. In Staff's view, the company's price predictions included in the MONET model were not reasonable assumptions, even for a placeholder value. Staff proposed to replace the placeholder value with the price of market energy for the four months for which an executed agreement does not currently exist (September-December 2017). If the PHP PPA is renewed before settlement of this AUT, Staff proposed the company update the value to reflect actual contract terms.

2. Stipulated Agreement

The price of the PHP PPA addressed in Staff's and ICNU's testimony will be set at the offered Qualifying Facility indicative pricing for the relevant months that PGE would receive output under the terms of the new PHP PPA, so that ratepayers will be made indifferent to whether PGE ultimately agrees to a new contract or purchases power from the market.

C. Boardman Rail Transportation Contracts

1. Parties' Original Positions

The Boardman plant receives coal through transportation agreements with BNSF Railway Company (BNSF) and the Union Pacific Railroad. These contracts require that a minimum number of tons of coal be shipped in 2017 and impose a liquidated damages charge for failure to meet the minimum requirement. PGE can partially manage this charge through coal stockpiling and, in the BNSF contract, rolling shipments into future years. PGE forecasts that it will be required to pay liquidated damages and proposed a change to MONET that dispatches based on the marginal cost of coal and would include these liquidated damages.

ICNU and Staff questioned the rollover tonnage assumption used by PGE. Staff agreed with PGE's method of modeling liquidated damages for the current AUT but proposed that PGE

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[3] ICNU/100, Mullins/4-5.

should not model liquidated damages attributable to 2016 or 2018. Staff proposed that inventory stockpile be modeled without change for calendar year 2017 and a zero rollover entering and leaving 2017. This would correctly attribute liquidated damage liabilities to the year in which they accrued. ICNU proposed that PGE set rollover tonnage into 2017 equivalent to the rollover tons into 2018.

2. Stipulated Agreement

The assumed BNSF rollover tons of coal from 2017 to 2018 will be set at an amount equal to the assumed rollover tons from 2016-2017. The assumed power costs will use a coal inventory level of 82 days of burn as the year-end 2017 assumption.

D. Coyote Forced Outage Rate

1. Parties' Original Positions

In docket UE 294, we addressed PGE's 2016 AUT as part of a general rate case. That filing included what Staff considered to be an excessive 2013 outage rate in the forced outage rate calculation for the Coyote Springs plant. The issue was resolved in a confidential settlement,[4] and it was not clear whether the company would continue to include the 2013 data in its forced outage rate calculation. PGE did include the data in its current AUT calculation.

ICNU opposed including the 2013 data for the reasons set forth in Staff's prior testimony and further argued that the length of the outage indicates imprudence on PGE's part. ICNU contends that PGE has not met its burden of proof to show the outage was prudent. Staff recommended removing the 2013 data from the four-year rolling average forced outage rate and substituting the 20-year historical average.

2. Stipulated Agreement

A forced outage rate of 7.0 percent will be used for the Coyote Springs plant.

E. Bonneville Power Administration (BPA) Transmission Rates

1. Parties' Original Positions

PGE's NVPC forecast filed on April 1, 2016, assumed a BPA transmission rate increase in the fourth quarter of 2017, based on the most current information available to it. PGE based its forecast of the Scheduling, System Control and Dispatch Service (SCD) rate on the current SCD rate multiplied by the average rate escalation for the seven BPA transmission rate case periods since fiscal year 2002.

ICNU questioned PGE's assumptions and proposed that PGE exclude a BPA transmission rate increase in the fourth quarter of the forecast period.

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[4] *In the Matter of Portland General Electric Company Request for a General Rate Revision*, Docket No. UE 294, Order No. 15-356, Appendix B at 4 (Nov 3, 2015).

2. *Stipulated Agreement*

PGE's assumed transmission rate increase in 2017 projected power costs will be reduced by $500,000.

F. Energy Imbalance Market (EIM) Benefits and Costs

1. *Parties' Original Positions*

PGE's testimony provided specific costs and benefits for its entry into the EIM market. CUB notes that PGE has assigned no value for EIM benefits therefore effectively forecasting them to be zero. While not offering a specific value, CUB stated it would review other parties' testimony to determine what the non-zero value should be. ICNU was not opposed to PGE's treatment. Staff believed that the company should have included the projection of costs and benefits even if they did turn out to be zero. By its own analysis, Staff did find a net benefit and therefore proposed a decrease in net power costs.

2. *Stipulated Agreement*

Test year power costs will include an EIM benefit of $1,011,000 and an EIM cost of $1,011,000. PGE will complete an EIM cost-benefit study to be used in its 2018 AUT filing. PGE agrees not to file for deferred accounting from the incremental costs associated with performing the study.

G. Wind Day Ahead Forecast Error

1. *Parties' Original Positions*

On June 9, 2016, PGE filed a letter with the parties indicating that the company was changing the methodology used to forecast the Day-Ahead Forecast Error from what was included in the initial filing. This change would change the cost from $0.20/MWh to $0.38/MWh. CUB argued that the modeling enhancement should be rejected because of the acknowledged agreement that modeling enhancements should be limited to the years that the company files a general rate case rather than in those years where an AUT is submitted.

2. *Stipulated Agreement*

The cost will be consistent with the cost included in PGE's April 1, 2016 NVPC forecast.

H. California – Oregon Border (COB) Trading Margins

1. *Parties' Original Positions*

PGE proposed to impose a minor restriction on the benefits of COB margins in the fourth quarter as a result of joining the EIM.

ICNU proposed lifting the restriction because no benefits associated with joining the EIM are reflected in the test period. ICNU asserted that lifting the restriction would result in a $0.1 million NVPC reduction.

Staff raised two concerns: first, the company was only modeling 87 percent of normal COB transactions and, second, PGE was using inconsistent methods to estimate price differentials. Staff proposed adjustments to PGE's cost estimate methodology to calculate the net benefit obtained from PGE's access to the COB market.

2. Stipulated Agreement

PGE's method for forecasting California trading margins will not change.

V. GENERAL AUT ISSUES DISCUSSION

We find that the stipulation is supported by competent evidence in the record, appropriately resolves the issues in the case, and results in just and reasonable rates.[5] Staff, ICNU, and CUB conducted a thorough investigation of the company's testimony and exhibits, served numerous data requests, participated in settlement conferences, and filed responsive testimony. Staff and all parties entered into the stipulation that resolves all relevant issues in the proceeding unrelated to PGE's long-term hedging proposal and have each executed the joint explanatory brief. No person has filed an objection to the stipulation.

We have examined the stipulation, the joint explanatory brief, and the pertinent record in the case. We find that the stipulation is supported by the record, which includes the company's testimony and exhibits describing the detailed calculations supporting Staff and intervenors' testimony thereon and the stipulated modifications to the AUT. We therefore conclude that the resulting rates are just and reasonable for resolution of the issues in this docket. The stipulation should be adopted in its entirety.

VI. PROPOSED LONG-TERM GAS HEDGING

We deny PGE's request to approve its proposed acquisition of a non-operating working interest in natural gas reserves. We conclude that the potential benefits to customers from this transaction are outweighed by the potential costs and risks of the venture. As a consequence, consistent with Staff's recommendation at the October 25, 2016 Public Meeting, we find that the related affiliated interest transactions in docket UI 376 are not fair and reasonable in all their terms and are contrary to the public interest. We therefore deny PGE's application for approval of the transactions and for waiver of the lower-of-cost-or-market rule in OAR 860-027-0048(4)(e). The Staff Report is attached as Appendix B.

Due to the limited time since the hearing on PGE's proposal, however, we are unable to prepare our complete written analysis explaining the rationale for our conclusion prior to PGE's requested deadline for an order. We will therefore issue a supplemental order providing a more complete summary of the long-term hedging proposal, the positions of the parties, and our reasons for denying this request.

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[5] *See, e.g., In the Matter of PacifiCorp, dba Pacific Power 2010 Transition Adjustment Mechanism,* Docket No. UE 207, Order No. 09-432 at 6 (Oct 30, 2009).

VII. ORDER

IT IS ORDERED that:

1. The stipulation between Portland General Electric Company, Staff of the Public Utility Commission of Oregon, the Citizens' Utility Board of Oregon, and the Industrial Customers of Northwest Utilities, attached as Appendix A, is adopted.

2. Portland General Electric Company must file its final MONET run on or before November 15, 2016, producing the final AUT Adjustment for 2017.

3. The request to include long-term natural gas hedging costs in the 2017 AUT is rejected.

4. The application for approval of affiliated interest transactions with Portland General Gas Supply Company and request for waiver of OAR 860-027-0048(4)(e), as submitted in docket UI 376, is denied.

5. Portland General Electric Company must file revised rate schedules consistent with this order to be effective no earlier than January 1, 2017.

Made, entered, and effective OCT 27 2016.

Lisa D. Hardie
Chair

John Savage
Commissioner

Stephen M. Bloom
Commissioner

PUBLIC UTILITY COMMISSION OF OREGON

A party may request rehearing or reconsideration of this order under ORS 756.561. A request for rehearing or reconsideration must be filed with the Commission within 60 days of the date of service of this order. The request must comply with the requirements in OAR 860-001-0720. A copy of the request must also be served on each party to the proceedings as provided in OAR 860-001-0180(2). A party may appeal this order by filing a petition for review with the Court of Appeals in compliance with ORS 183.480 through 183.484.

ORDER NO. 16 419

BEFORE THE PUBLIC UTILITY COMMISSION

OF OREGON

UE 308

In the Matter of PORTLAND GENERAL ELECTRIC COMPANY's 2017 Annual Power Cost Update Tariff	**STIPULATION**

This Stipulation ("Stipulation") is among Portland General Electric Company ("PGE"), Staff of the Public Utility Commission of Oregon ("Staff"), the Citizens' Utility Board of Oregon ("CUB"), and the Industrial Customers of Northwest Utilities ("ICNU") (collectively, the "Stipulating Parties").

I. INTRODUCTION

On April 1, 2016, PGE filed its annual power cost update as required by Tariff Schedule 125. That filing included testimony and work papers, and the information required by the minimum filing requirements ("MFRs"). PGE's filing also included a long-term gas hedging proposal.

The Commission adopted two schedules in this docket, one for the long-term gas hedging proposal, and the other for all other power cost issues. The parties in this docket sent and PGE responded to data requests. PGE has filed, and will continue to file, updates to its power costs in accordance with the schedule set by the ALJ in this docket. Staff, CUB, and ICNU filed testimony on power cost issues on June 20, 2016. Noble Americas Energy Solutions ("Noble") is also a party to this docket but did not file testimony. The Stipulating Parties held a settlement conference on June 27, 2016. As a result of those discussions, the Parties have reached agreement settling all issues raised in this proceeding except those regarding the long-term gas hedging proposal. Noble did not participate in settlement discussions and does not object to this Stipulation. The Stipulating Parties request that the Commission issue an order adopting this Stipulation.

II. TERMS OF STIPULATION

1. This Stipulation settles all issues in this docket except those regarding the long-term gas hedging proposal.

2. Portland Hydro Project Expiration. Forecasted costs in PGE's 2018 AUT will reflect the assumption that PGE will receive a refund from the City of Portland related to the expiration of the Portland Hydro Project PPA in the amount of $9.4 million. If PGE receives an amount different from $9.4 million in 2018 (or the year prior), the difference between this forecasted amount and the actual amount received by PGE will be included, with interest, in PGE's 2019 AUT.

3. PPA Price. The price of the PPA addressed in Staff's and ICNU's testimony will be set at the offered Qualifying Facility indicative pricing for the relevant months that PGE would receive output under the terms of the new PPA.

4. Boardman Rail Transportation Contracts. For purposes of this docket, the assumed BNSF Railway Company rollover tons of coal from 2017 to 2018 will be set equal to the assumed rollover tons from 2016 to 2017. For purposes of this docket, power costs will use a coal inventory level of 82 days of burn as the year-end 2017 assumption.

5. Coyote Forced Outage Rate. For purposes of this docket, a forced outage rate of 7.0% will be used for the Coyote Springs plant.

6. BPA Transmission Rates. 2017 projected power costs will be reduced by $500,000.

7. Other Issues. In settlement of issues related to EIM Benefits and Costs, California Trading Margins, and Wind Day Ahead Forecast Error, parties agree to the following:

a. Test year power costs will include an EIM benefit of $1,011,000 and an EIM cost of $1,011,000.

b. PGE will complete an EIM cost-benefit study to be used in its 2018 AUT filing. PGE agrees not to file for deferred accounting for the incremental costs associated with performing the study.

c. Wind Day Ahead Forecast Error cost will be consistent with the cost included in PGE's April 1, 2016, net variable power cost forecast.

8. This settlement is not precedential as to any issue or party, except as otherwise provided in the settlement.

9. The Parties recommend and request that the Commission approve the adjustments described above to PGE's 2017 power costs as appropriate and reasonable resolutions of the issues settled herein.

10. The Stipulating Parties agree that this Stipulation is in the public interest and will result in rates that are fair, just and reasonable and will meet the standard in ORS 756.040.

11. The Stipulating Parties agree that this Stipulation represents a compromise in the positions of the parties. Without the written consent of all parties, evidence of conduct or statements, including but not limited to term sheets or other documents created solely for use in settlement conferences in this docket, are confidential and not admissible in the instant or any subsequent proceeding, unless independently discoverable or offered for other purposes allowed under ORS 40.190.

12. The Stipulating Parties have negotiated this Stipulation as an integrated document. If the Commission rejects all or any material part of this Stipulation, or adds any material condition to any final order that is not consistent with this Stipulation, each Stipulating Party reserves its right (i) to withdraw from the Stipulation, upon written notice to the Commission and other Parties within five (5) business days of service of the final order that rejects this Stipulation, in whole or material part, or adds such material condition; (ii) pursuant to OAR 860-001-0350(9), to present evidence and argument on the record in support of the Stipulation, including the right to cross-examine witnesses, introduce evidence as deemed appropriate to respond fully to issues presented, and raise issues that are incorporated in the settlements embodied in this Stipulation; and (iii) pursuant to ORS 756.561 and OAR 860-001-0720, to seek rehearing or reconsideration or to appeal the Commission order under ORS 756.610. Nothing in this paragraph provides any Party the right to withdraw from this Stipulation as a result of the Commission's resolution of issues that this Stipulation does not resolve.

13. This Stipulation will be offered into the record in this proceeding as evidence pursuant to OAR § 860-01-0350(7). The Stipulating Parties agree to support this Stipulation throughout this proceeding and in any appeal, provide witnesses to support this Stipulation (if specifically required by the Commission), and recommend that the Commission issue an order adopting the settlements contained herein. The Stipulating parties also agree to cooperate in drafting and submitting an explanatory brief and written testimony per OAR § 860-001-0350(7), unless such requirement is waived. By entering into this Stipulation, no Stipulating Party shall be deemed to have approved, admitted or consented to the facts, principles, methods or theories employed by any other Party in arriving at the terms of this Stipulation. Except as provided in this Stipulation, no

Stipulating Party shall be deemed to have agreed that any provision of this Stipulation is appropriate for resolving issues in any other proceeding.

14. This Stipulation may be signed in any number of counterparts, each of which will be an original for all purposes, but all of which taken together will constitute one and the same agreement.

DATED this 18th day of August, 2016.

PORTLAND GENERAL ELECTRIC COMPANY

STAFF OF THE PUBLIC UTILITY COMMISSION OF OREGON

CITIZENS' UTILITY BOARD OF OREGON

INDUSTRIAL CUSTOMERS OF NORTHWEST UTILITIES

Stipulating Party shall be deemed to have agreed that any provision of this Stipulation is appropriate for resolving issues in any other proceeding.

14. This Stipulation may be signed in any number of counterparts, each of which will be an original for all purposes, but all of which taken together will constitute one and the same agreement.

DATED this 17th day of August, 2016.

PORTLAND GENERAL ELECTRIC COMPANY

STAFF OF THE PUBLIC UTILITY COMMISSION OF OREGON

CITIZENS' UTILITY BOARD OF OREGON

INDUSTRIAL CUSTOMERS OF NORTHWEST UTILITIES

Stipulating Party shall be deemed to have agreed that any provision of this Stipulation is appropriate for resolving issues in any other proceeding.

14. This Stipulation may be signed in any number of counterparts, each of which will be an original for all purposes, but all of which taken together will constitute one and the same agreement.

DATED this 8 day of August, 2016.

PORTLAND GENERAL ELECTRIC COMPANY

STAFF OF THE PUBLIC UTILITY COMMISSION OF OREGON

CITIZENS' UTILITY BOARD OF OREGON

INDUSTRIAL CUSTOMERS OF NORTHWEST UTILITIES

Stipulating Party shall be deemed to have agreed that any provision of this Stipulation is appropriate for resolving issues in any other proceeding.

14. This Stipulation may be signed in any number of counterparts, each of which will be an original for all purposes, but all of which taken together will constitute one and the same agreement.

DATED this 5th day of August, 2016.

PORTLAND GENERAL ELECTRIC COMPANY

STAFF OF THE PUBLIC UTILITY COMMISSION OF OREGON

CITIZENS' UTILITY BOARD OF OREGON

INDUSTRIAL CUSTOMERS OF NORTHWEST UTILITIES

ORDER NO. 16 419

ITEM NO. 1

PUBLIC UTILITY COMMISSION OF OREGON
REDACTED STAFF REPORT
PUBLIC MEETING DATE: October 25, 2016

REGULAR X **CONSENT** ____ **EFFECTIVE DATE** ____________

DATE: October 17, 2016

TO: Public Utility Commission

FROM: Lance Kaufman LK

THROUGH: Jason Eisdorfer and Marc Hellman JE MH

SUBJECT: PORTLAND GENERAL ELECTRIC: (Docket No. UI 376) Application for Affiliated Interest Transactions related to Gas Reserves.

STAFF RECOMMENDATION:

The Affiliated Interest contract, guarantee of indebtedness and waiver of the lower of cost or market rule are necessary components of Portland General Electric Company (PGE)'s investing in gas reserve costs at issue in Docket No. UE 308. If the Commission allows gas reserve costs into rates in Docket No. UE 308, the Commission should also find that the Affiliated Interest contract is fair, reasonable, and in the public interest; approve the guarantee of indebtedness; and waive the lower of cost or market rule. The Commission should also adopt Staff's proposed deferral treatment and the reporting requirements identified by Staff in this memo.

Should the Commission decline to allow gas reserve costs into rates in Docket No. UE 308, the Commission should find the Affiliated Interest contract is not in the public interest, disapprove the guarantee of indebtedness, and not waive the lower of cost or market rule.

Due to the 90-day statutory period for review of the Affiliated Interest Agreement in this docket discussed below, which expires on November 3, 2016, the Commission should make a decision regarding this docket concurrently with the decision in Docket No. UE 308. The procedural schedule in Docket No. UE 308 contemplates Commission order in this case by November 4, 2017.

DISCUSSION:

Issue
Whether to approve PGE's Affiliated Interest contract, guarantee of indebtedness, and request for waiver of OAR 860-027-0048.

Applicable Law
PGE filed this application with the Commission on August 5, 2016, pursuant to OAR 860-027-0040, OAR 860-027-0041, ORS 757.015 and ORS 757.495. Staff also finds that OAR 860-001-000, OAR 860-027-0035, OAR 860-027-0048, and OAR 860-027-0100 are relevant to this application.

I. OAR 860-027-0040 addresses filing requirements for applications for approval of transactions between Affiliated Interests.

II. OAR 860-027-0041 identifies information required for utility goods or services provided to Affiliated Interests.

III. ORS 757.015 defines Affiliated Interests.

IV. ORS 757.495 addresses Utility and Commission treatment of Affiliated Interest Contracts.

V. OAR 860-027-0000(2) provides the Commission authority to waive any rule in Division 27 for good cause shown.

VI. OAR 860-027-0035 addresses filing requirements for applications by a utility for authority to guarantee indebtedness.

VII. OAR 860-027-0048 requires that a utility's costs to purchase goods or services from an Affiliated Interest must be recorded in the utility's books at the lower of cost or market.

VIII. OAR 860-027-0100 requires annual reporting of Affiliated Interest transactions.

This filing consists of three parts, an Affiliated Interest contract, a guarantee of indebtedness by PGE of the Affiliate's debt, and a waiver of the lower of cost or market provision in OAR 860-027-0048(4)(e). ORS 757.495(3) requires that the Commission investigate the Affiliated Interest contract and determine if the contract is fair and reasonable and not contrary to the public interest. ORS 757.495(5) requires that the

Commission indicate approval or disapproval of the guarantee of indebtedness. OAR 860-027-0000(2) allows the Commission to waive OAR 860-027-0048(4)(e) for good cause.

Discussion and Analysis

In this filing Portland General Electric is applying for Commission approval of Affiliated Interest transactions with Portland General Gas Supply Company (PGGS). The transactions facilitate the PGE proposal at issue in PGE's Automatic Update Tariff (AUT) proceeding to recover costs of a capital investment in gas reserves through a cost-of-service purchase gas agreement with its affiliate. PGE has timed this filing to allow the Commission's findings to be concurrent with those in PGE's AUT proceeding, Docket No. UE 308. PGE has provided testimony on and included costs related to PGGS in Docket UE 308. Staff, Citizens' Utility Board of Oregon, and Industrial Customers of Northwest Utilities have provided testimony regarding the PGE/PGGS transactions in Docket UE 308. The Commission held a Hearing on September 21, 2016. The Commission questioned witnesses at that Hearing.

Docket UE 308 is a contested case, contains testimony from PGE's major stake holders, and has a more thorough record regarding the gas reserve investment relative to this Docket. The Commission should rely on the record developed in Docket No. UE 308 when making findings regarding the fairness, reasonableness, and public interest of PGE's proposed cost-of-service gas production investment.

The final order for UE 308 is scheduled for November 4, 2016. The statutory deadline for the Commission to make findings regarding this docket is November 3, 2016.[1] The timing of these dockets allows the Commission's findings in this Docket to be concurrent and consistent with the Commission's findings in Docket No. UE 308. If the Commission decision in UE 308 does not allow costs related to the gas reserve investment into rates, a consistent decision in this docket would be to find the Affiliated Interest contract is not in the public interest, to disapprove the guarantee of indebtedness, and to not waive the lower of cost or market rule.

Should the Commission rule in favor of the Company in UE 308, a consistent ruling in this docket would be to find the Affiliated Interest contract is in the public interest, to approve the guarantee of indebtedness, and to waive the lower of cost or market rule.

The record in Docket No. UE 308 does not include Staff's analysis or recommendations specific to PGE's Affiliated Interest contract, reporting requirements, or waiver of OAR 860-027-0048(4)(e). In this memo, Staff provides specific recommendations if the

[1] ORS 757.495 provides the Commission with 90 days from the filing date to make findings regarding Affiliated Interest contracts.

Commission choses to include the proposed gas reserve investments into rates in Docket No. UE 308.

Fairness of Contract
In Docket No. UE 308, Staff found PGE's proposal to be unfair due to intergenerational subsidization, whereby current customers subsidize future customers. PGE's argument in favor of the gas reserve investment is that it will reduce long term gas risk. Staff argues that alternate and preferable financial instruments are available to reduce gas risk up to 10 years.

Staff proposes deferred accounting treatment of the portion of the cost of service gas that is above the forecasted cost of gas. Such treatment would defer the portion of the cost of service gas costs that are above the initially forecasted gas price. This treatment consistently aligns the costs of the investment with the primary time period of the incremental benefit of the gas reserve investment over a traditional financial hedge. If the Commission supports Staff's proposed deferral treatment, the Commission should direct Staff, PGE, and any interested party to collaborate in developing a proposal for later ratemaking treatment of the deferred amounts that aligns the costs and benefits of the gas reserve investment without harming PGGS or PGE.

Public Interest of Contract
In Docket No. UE 308 Staff found PGE's proposal to be speculative and not likely to increase rate stability. Staff also found that alternate gas hedging mechanisms would provide customers with greater rate stability without exposing customers to additional risk. For these reasons Staff found that the proposal presented in Docket No. UE 308 is not in the public interest.

The proposal in this docket is directly related to the proposal in Docket UE 308. If the Commission rules in favor of the Company in Docket UE 308, than the Commission is implicitly ruling that the Affiliated Interest contract is in the public interest. This is because the Affiliated Interest contract is an integral part of the gas reserve investment, and the investment will not be undertaken without approval of the Affiliated Interest contract.

Affiliate Reporting Requirements
PGE's proposed gas reserve investment is a new and uncommon electric utility investment. Due to the controversial nature of the investment, and PGE's intention **[Begin Confidential]** [redacted], **[End Confidential]** the Company should present operational reports that contain more detail than the general Affiliated Interest report. Staff recommends the annual reports contain the following information.

A. Side by side comparison of actual values, initial (investment decision perspective) forecast, and AUT forecast of production volumes and cost-of-service gas prices.

B. Actual and last three years side-by-side comparison of:
   i. Production volume
   ii. Cost of service gas price
   iii. Summary of production costs on a total and per unit basis
   iv. Sale prices and quantities for marketed gas and liquids
   v. Detailed trial balance
   vi. Income statement

C. Current year only reporting of:
   i. Hedge comparison report matching cost of gas from PGGS to market indicators (spot, near futures, swaps).
   ii. General ledger as a work paper
   iii. Risk report (Spills, fines and citations, new regulations, etc.)

The annual reporting will be satisfied with two separate reports. PGE will provide PGGS production, cost, sales, and market detail with PGE's AUT filing by April 1. PGE will provide PGGS financial detail with PGE's Affiliated Interest Report by June 1.

PGE has proposed a five-year review of the gas reserves drilling program. After five years, PGE will provide a reassessment report as part of a docketed proceeding in order to allow other parties the opportunity to comment. The report will evaluate how PGGS's hedging results have been trending. As noted in UE 308 PGE Exhibit 200, PGE would expect, after the initial five-year period, a Commission decision regarding ratemaking treatment of the gas reserve investment that would indicate one of the following:

- Reauthorize PGE's long-term gas hedging as currently operating;
- Reauthorize PGE's long-term gas hedging program but with modifications to the program or additional conditions/guidelines; or
- Decline to authorize any additional long-term gas hedging agreements or transactions while continuing to permit recognition in rates natural gas acquired under prior transactions.

Guarantee of Indebtedness
PGE currently has sufficient liquidity to satisfy the proposed guarantee of indebtedness. **[Begin Confidential]** [redacted]

[redacted] **[End Confidential]**

For these reasons Staff finds the guarantee to be reasonable. Should the Commission find in favor of the gas reserve investment, the Commission should approve the guarantee of indebtedness.

Waiver of Lower of Cost or Market Rule
OAR 860-027-0000(2) provides the Commission authority to waive Division 27 rules for good cause shown. If the Commission approves cost-recovery of the gas reserve investment in Docket No UE 308, Staff recommends that the Commission approve PGE's request to waive the requirement that PGE record its costs associated with the PGGS contract at the lower of cost or market. According to the Company, **[Begin Confidential]** [redacted] **[End Confidential]** and PGE's Power Cost Adjustment help protect customers from significant cost changes due to deviations in production. As such, a waiver of the lower-of-cost-or-market rule is necessary for cost of service gas prices.

Conclusion
Staff makes the following recommendations to the Commission:

The Commission should make a decision regarding this docket concurrently with the decision in Docket No. UE 308. Should the Commission allow gas reserve costs into rates in Docket No. UE 308, the Commission should also find that the Affiliated Interest contract is in fair, reasonable, and in the public interest; approve the guarantee of indebtedness; and waive the lower of cost or market rule. The Commission should also adopt Staff's proposed deferral treatment and the reporting requirements identified by Staff in this memo.

Should the Commission decline to allow gas reserve costs into rates in Docket No. UE 308, the Commission should find the Affiliated Interest contract is not in the public interest, disapprove the guarantee of indebtedness, and not waive the lower of cost or market rule.

PROPOSED COMMISSION MOTION:

Make findings in this Docket concurrently with Docket No. UE 308 and adopt Staff's recommendations in the Staff Memo for this docket.

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